No. 7966

In the United States Circuit Court of Appeals

For the Ninth Circuit.

Samuel S. Gelberg, Attorney for Creditors Committee of Western Blind & Screen Co., a corporation, also known as Western Venetian Blind Co., a corporation, and Creditors Committee for Western Blind & Screen Co., also known as Western Venetian Blind Co., a corporation,

Appellants,

vs.

E. C. Richardson, Receiver for Western Blind & Screen Co., a corporation, also known as Western Venetian Blind Co., a corporation,

Appellee.

BRIEF OF APPELLANTS.

SAMUEL S. GELBERG,
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Attorney for Creditors Committee and Creditors Committee of Western Blind and Screen Co., Inc., a corporation, Appellants.

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BRIEF OF APPELLANTS.

The questions under consideration before this Honorable Court may be stated as follows:

1. *Did the District Court err in denying the Intervening Petition of Samuel S. Gelberg, attorney for the Creditors Committee, for Allowance of Compensation and the Intervening Petition of the Creditors Committee for Allowance of Expense?*

2. *Did the District Court err in finding that there was no showing that the estate had been enriched but only preserved through the efforts of said Samuel S. Gelberg, attorney for the Creditors Committee and the Creditors Committee?*

3. *Did the District Court err in finding that in the absence of a showing that the estate has been increased, rather than preserved, allowance cannot properly be made in this case?*

4. *Did the District Court err in refusing to hear or consider the offer of Samuel S. Gelberg, attorney for the Creditors Committee and the Creditors Committee, respectively, to present testimony, evidence, and proof of services rendered by said attorney for Creditors Committee and the Creditors Committee in support of their petitions?*

I.

The Court May Allow Fees Out of the Administration of the Estate to the Attorney or the Creditors Committee Compensating Him, or It, for the Work Done in Enriching or Preserving the Estate.

Both the petitions of Samuel S. Gelberg, attorney for the Creditors Committee [Tr. p. 40] and the petition of the Creditors Committee itself [Tr. p. 31], set forth a recital of the services rendered by said attorney and said Committee whereby the estate was enriched, enhanced, and preserved, none of which is disputed. *We therefore start with the premise that the estate was enriched by the release of fifteen thousand dollars ($15,000.00) in accounts receivable which had been assigned by the respondent corporations to Mrs. D. L. Gripton, an officer of the*

said corporations, to secure claims of said Mrs. Gripton in the amount of forty-one thousand dollars ($41,000.00) against said corporations. It is also conceded and has not at any time been disputed or denied by anyone in this proceeding, that without the release of said fifteen thousand dollars ($15,000.00) the business of the respondent corporations could not have operated, and would have had to be liquidated in forced sale with resulting loss to creditors. [Tr. p. 34.] It was through the operation of the business of the corporations that said business was kept alive until a fire consumed the plant of the respondent corporations and the proceeds of the insurance, which were realized by the Receiver, were sufficient to permit a payment of a twenty per cent (20%) first dividend to creditors with an ultimate prospect of eventual payment of sixty per cent (60%) in dividends, in addition to administration expenses, including the expenses of the attorneys for the Creditors Committee. [Tr. p. 37.]

It is further conceded and admitted by the parties to this proceeding that the efforts of Samuel S. Gelberg, attorney for the Creditors Committee were instrumental in securing the release of said fifteen thousand dollars ($15,000.00) by Mrs. Gripton. [Tr. p. 34.]

Authorities.

The principle expressed by the United States Supreme Court in *Trustees v. Greenaugh*, 105 U. S. 527, wherein an allowance was made out of the common trust funds of the estate, has been generally followed by the Supreme Court of the United States and the Circuit Courts of Appeal, in matters of this kind:

"It is a general principle that a trust estate must bear the expenses of its administration. It is also established by sufficient authority, that where one of many parties having a common interest in a trust fund, at his own expense takes proper proceedings to save it from destruction and to restore it to the purposes of the trust, he is entitled to reimbursement, either out of the fund itself, or by proportional contribution from those who accept the benefit of his efforts."

And in the same case, at page 532:

"*To make them a charge upon the fund is the most equitable way of securing such contribution.*" (Italics ours.)

Again at page 536:

"Still, a just respect for the eminent judges under whose direction many of these cases have been administered would lead to the conclusion that allowances of this kind, if made with moderation and a jealous regard to the rights of those who are interested in the funds, are not only admissible, but agreeable to the principles of equity and justice."

Cuyler, et al. v. Atlantic and N. C. R. Co., 132 U. S. 570, quoting from syllabus:

"A federal Court of Equity has power to make an allowance for counsel fees to a complainant who, as a joint owner of a fund or property has maintained a suit for its preservation or protection, where it has brought within the custody or control of the court, such allowance to be charged thereon;".

From the same case:

> "This syllabus of the case" (referring to the *Greenaugh* case) "is cited with approval in numerous decisions, both by the Supreme Court of the United States and by the Circuit Court of Appeals in several of the circuits, and seems to be the settled law on the subject."

Central R. R. v. Pettus, 113 U. S. 122;
Harrison v. Perea, 168 U. S. 326;
Dodge v. Tulleys, 144 U. S. 457;
Medaugh v. Wilson, 151 U. S. 351.

In the case of *Medaugh v. Wilson, supra,* assignees (apparently synonymous with trustees in bankruptcy today) were allowed expenses and compensation of their counsel for preserving certain assets even though said assets were not in their possession and they were in fact outsiders to the receivership proceedings. To quote from the case itself:

> "Their services in this respect not being to any party or parties but in respect to the property itself and to secure its proper application among all parties interested, it is clearly in accordance with settled rules of equity jurisprudence, as well as with the practice in bankruptcy proceedings, that the compensation for their services, including the pay of their counsel, should be made a direct charge upon the property, and a charge prior in right to the claims of creditors or stockholders. 'It is a general principle that a trust estate must bear the expenses of its administration'."

This principle is clearly applicable to the status of this applicant. As in the above case, it is not to the parties or creditors that the services were rendered by your petitioner but in respect to the property itself, although the creditors were directly benefited by such services and the broad principles of equity should be applied and the cost of said services equally apportioned among all beneficiaries.

In *Louisville E. & St. L. R. Co. v. Wilson,* 138 U. S. 501, the court held, where there are no surplus earnings, an attorney who recovers for a railroad, in the hands of a Receiver, engines formerly leased by it to another road, and rent for their use, is entitled to a reasonable compensation to be paid out of the *corpus* of the property, as the benefit of the recovery inured to the security holders.

In *William Furth Co. v. Millen Cotton Mills,* 129 Fed. 141, where in foreclosure action petitioners filed a bill on behalf of certain stockholders as result of which a previous sale was set aside, resulting in a resale of assets at an increased price, the petitioners having rendered valuable services both to the court and the creditors, were entitled to a fee out of proceeds of the sale.

A court may properly make allowances of fees to solicitors for services rendered before it upon its own knowledge as to the extent and value of such services.

Colley v. Wolcott, 197 Fed. 595.

In *Hein v. Gravelle Farmers' Elevator Co.,* 2 Pac. (2d) 741, at page 745, the court said, with regard to application for fees of successful objectors to insolvent Receiver's allowance of invalid claim:

> "Although the objections and defenses made by the respondents did not actually create or augment an

> estate, it certainly preserved the estate for lawful creditors of the insolvent company. . . . They have incurred expense which resulted in benefits to others interested in the estate, and we think should receive some reasonable compensation."

Thus the courts of equity go even further and allow for expenses incurred in merely preserving assets already in existence as well as for creating or increasing the common fund. So, in this case, even if the funds of the estate had not been enhanced, the attorney for the Creditors' Committee would still have been entitled to compensation as an expense of the committee, for by its constant vigilance, its participation in the affairs of the estate, both in and out of court, its cooperation with the Receiver, its objections actively to the claim of Mrs. Gripton to forty-one thousand dollars ($41,000.00) in securities, its objection to certain allowances, and in helping to keep the business going, it has preserved this estate for the benefit of all creditors.

Wagoner Oil & Gas Co. v. Marlow, 278 Pac. 294, at page 309:

> "Receivership expenses, in the absence of statute, should in all cases, as between the parties, be adjusted upon equitable principles."

The Creditors Committee is a party to this proceeding, its petition for intervention having been allowed upon order of court duly made herein [Tr. p. 12]. *The equitable principle above quoted therefore applies to expenses incurred by this committee, as well as other parties.*

A case where outside attorneys employed by regularly employed attorneys for the Receiver were allowed fees

as part of the administration expense under certain circumstances over objections is

> *In re Dissolution of Henry Smith Floral Co.,* 244 N. W. 480;

further indicating how far the courts will go in allowing compensation as an expense of administration.

Goodwin v. Milwaukee Lithographing Co., 177 N. W. Rep. 618, is a case where the intervening petitioner rendered valuable services in prosecuting the action and by their efforts contributed to the *conservation* of the fund. It was held in that case that it was within the power of the court to provide for the reimbursement of said intervention.

Morgan, et al. v. Grass, Fibre, Pulp and Paper Corporation, 11 Fed. (2d) 431:

> "It is the recognized law that, where one creditor, acting for himself and other creditors, succeeds in bringing into court a fund to be administered for the satisfaction of his claim and the claims of other creditors of the like class, he is allowed a reasonable fee for his solicitor, to be paid out of such fund."

In the matter of *Robinson v. Mutual Reserve Life Insurance Co.,* 189 Fed. 347 (C. C. A. 2nd Circuit, 1911), the court said:

> "Where a complicated controversy involving many different interests in a fund is before the court and some particular interest is not so represented that the facts supporting its claim are likely to be fully brought out and properly presented, we know of no reason why the court may not assign some competent person to do the work, and compensate him as Receiver's Counsel is compensated, viz, out of the

funds in the hands of the Receiver. *We think it would be unfortunate if the Courts did not possess such power, because the Receivers necessarily represent so many different interests that they must generally stand neutral, and there will be many occasions where correct conclusions can be reached only after all sides of the controversy have been vigorously presented.*" (Italics ours.)

In the case of *Robinson v. Mutual Reserve Life Insurance Co.*, 182 Fed. 850, at p. 863, an outstanding case on this subject, the court (Circuit Court, S. D. N. Y., November 7th, 1910) says:

> "Mr. Lewis, on the other hand, intervening for Elizabeth A. Sharman, did obtain for his clients and others similarly situated, the sum of Fifteen Thousand Dollars ($15,000.00) by taking it out of the funds in Court, adversely to the Receivers on the ground that they did not deserve it. This would amount, I think, to the creation of a fund in court adversely to the Receivers on the ground that they never were entitled to it. This would amount, I think, to the creation of a fund, and I think he is entitled to an allowance of One Thousand Dollars ($1,000.00) to be deducted ratably from the sums going to the participants in that fund."

Burden Co. v. Ferris Co., 87 Fed. 810, 31 C. C. A. 233;

Pennsylvania Steel Co. v. New York City Railway Co., 221 Fed. 440.

The court, in its decision [Tr. p. 50] denying the petition of the attorney and the Creditors Committee apparently has done so on the theory that it is only in the cases where the estate has been *increased* rather than *pre-*

served that an allowance can properly be made under the law. *It will be noted that nowhere in the cases above cited, is there any differentiation made between a preservation or conservation and an enrichment or an enhancement.* In principle and effect we cannot see any difference in the use of the terms so far as the point in question is concerned. In either case, the ultimate returns to the interested parties are increased through said efforts, whether they bring a preservation or an enrichment. As a matter of fact, all cases of allowances to attorneys for the complainant in receivership matters are actually allowed on the theory of *preservation* of the common fund.

II.

The Court May Instruct the Receiver to Pay the Bill for Services Rendered to the Creditors Committee by Its Attorney Out of the Common Fund to Be Distributed to Creditors.

It should be noted that although notice by publication and by mail, in accordance with the order of the court, was given to all creditors and interested parties, of the petition for instructions by receiver [Tr. p. 30], no objections were filed or made in open court by anyone prior to or at the time of the hearing of said petition of the attorney for the Creditors Committee and of the Creditors Committee itself on February 4th, 1935.

The intervening petition of the Creditors Committee [Tr. p. 32] sets forth that it was chosen after due notice to all creditors and after a copy of the minute order directing the creation of such committee was sent to each creditor. It was obvious that the order directing the creation of the committee was for the purpose of pro-

tecting the rights of the creditors and as a check on the expenditures and policy of the Receiver. It is further obvious that the order contemplated the services of an attorney and such employment flowed naturally from the performance of its duties and functioning of said committee. *The estate is a fund which will eventually be distributed to the creditors represented by this committee; a common fund. The Creditors Committee in equity should be allowed to draw against such common fund in order to pay expenses which flow naturally from the performance of its duties as the committee.*

Analogous to this theory is Section 77 B (C-8) of the Bankruptcy Act recently enacted by Congress which provides for compensation to creditors committees and their attorneys.

To say that the attorney having rendered valuable services in connection with the preservation of creditors' rights and actual enhancement of creditors' funds must collect his fee proportionately from each individual creditor under the foregoing circumstances would not be equity, and is a practical impossibility with creditors scattered all over the states. Besides, the payment of this fee out of the creditors' common fund amounts in effect to the same thing as collecting it from each individual creditor, only in the most logical and practical manner.

In conjunction with the administration of the estate the court took the precaution of providing for the protection of creditors' rights by ordering the creation of this committee. The creditors, through this committee, to make its functioning possible, employed an attorney and now petitions this court to allow it to draw on the common fund of the creditors to compensate the said attorney the fair and reasonable amount of $1,250.00.

It should be observed by the court as of considerable importance that the membership of the Creditors Committee is in itself composed of the largest creditors and that the members *in themselves* represent about 70% of the total indebtedness. We therefore have the *express consent* of about 70% of those ultimately entitled to receive the funds in the hands of the Receiver. The balance of about 30% have in *two ways* consented to the payment of this expense: (1) By selecting this committee as their true representative in connection with the administration of this estate and thereby making its acts their acts; and (2) By not objecting to such allowance after due notice and therefore impliedly consenting to such allowance. Thus we have the remaining 30% of the creditors actually sanctioning and affirming the act of the committee in authorizing this allowance. *We therefore have the actual consent of the only parties who will be affected by the allowance, the creditors.* Any question of the fairness of the amount requested must be dismissed, in view of the fact that the committee itself will be most affected by the allowance, since it represents among its members, the greater part of the total indebtedness of the respondents. It is a common practice for allowance to be made to the attorney for a Creditors Committee in matters of reorganization or compositions in the winding up of corporate receiverships, where such allowance is stipulated or agreed upon by all interested parties. The situation here is analogous. *The Committee is simply asking the court to sanction what has already been agreed upon by those concerned and interested in the common fund.* Certainly there cannot be any objection on the part of the court to any such voluntary arrangement. Such procedure has been repeatedly sanctioned and approved by the courts.

III.

The District Court Erred in Refusing to Hear or Consider Testimony and Proof of Services.

When the petitions of the Creditors Committee and *Samuel S. Gelberg,* as attorney for the Creditors Committee, came up for hearing on February 4, 1935, pursuant to order to show cause on all interested parties and creditors why said fees or expenses should not be allowed, the court's refusal to hear or consider the offer of said attorney in his own behalf or in behalf of the Creditors Committee to present testimony, evidence and proof enlarging upon the services rendered by said attorney and said committee, obviously constituted error on the part of the court. It does not seem necessary to submit any authorities on the subject, as at least it was an abuse of discretion. The only construction that might be placed upon such refusal was that the court did not require any further proof or evidence of said services, being satisfied that the same were as set forth in the respective petitions.

ARGUMENT AND CONCLUSION.

The release of fifteen thousand dollars ($15,000.00) by Mrs. D. L. Gripton to the Receiver was the relinquishment by her of a positive property right in said funds. This money was not a part of the estate when the Receiver was appointed, but was held by her as her personal property by virtue of a written assignment by the respondent corporations, and its release, which was forced by the appellant added to or increased the funds in receivership to the extent of fifteen thousand dollars ($15,000.00). There is no other possible conclusion.

A particular and important distinction must be taken into consideration as distinguishing this Creditors Committee from the usual one. This is not a voluntary committee such as is sometimes formed by groups of creditors; but is a duly appointed committee created by order of court at the express request of the court made simultaneously with the appointment of the Receiver and as such represents *all creditors.* The purpose of creating this committee as expressed by the order was to so act as to preserve the estate for the benefit of the creditors and to act as a check on the Receiver. It is therefore impossible to understand how these assigned duties could be successfully carried out in receivership operating a large business over a long period of time, involving innumerable complications and problems such as complete absence of necessary finances, threatened foreclosures, matters of policy, allowances to Receivers and attorneys, complicated and voluminous auditors' reports, plans for reorganization involving the interests of creditors, liquidations, etc., without the aid of counsel skilled in the law and especially in such matters. That the committee was successful in this case largely through the efforts and labor of their attorney is clearly affirmed by their prayer for allowance of fair and reasonable compensation to said attorney.

It is conceded and has been held repeatedly by the decisions that the position of Receiver in Equity is a neutral one, as the custodian appointed by the court, and as such is the arm of the court and represents not only the cred-

itors but also the corporations in receivership. In the case under consideration, the Receiver was, prior to his appointment, the general sales manager of the corporation and was appointed upon the consent of the creditors and the approval of the respondent corporations. It was, therefore, necessary and advisable that the creditors as a group be represented. As has been seen from the cases that have been cited, Courts of Equity have always encouraged and rewarded the services, whether voluntary or otherwise, of any party to such a proceeding whereby the estate or the funds of the estate are preserved or enhanced in value. It appears to us that it would be dangerous to discourage class representation and participation of creditors in the administration of estates.

It is true that the power to allow compensation and expenses in cases of this kind should be exercised with caution and with regard to the value of services rendered to creditors and to the estate, but is likewise true that in a proper case, a party through whose efforts the estate is preserved or enhanced, should be compensated for his diligence, thus encouraging efforts of this kind as most important to the estate and those interested therein.

The Federal Legislature in enacting section 77B (C-8) of the Bankruptcy Act, whereby express provision is made for compensation to creditors committee and attorneys representing various classes of creditors, undoubtedly had in mind the importance to creditors of an insolvent debtor, that all parties be encouraged to work for the preservation and the reorganization of the debtor rather

than to passively permit the estate to be liquidated and the assets to be sold at forced sale at a fraction of their actual worth with resulting heavy losses to the creditors, to the debtor, and to the community. The present tendency, and one to be encouraged, is not to sit back and let nature take its course *but to do something about it;* to make an active and determined effort to prevent a failure, to preserve rather than to destroy an institution. Therein is recognized the fact that the failure of an established business is a distinct loss to the community. The desire to plan and achieve a reorganization should be encouraged rather than to be rebuffed. Destroy the possibility of compensation for such services to the creditors committees in proper cases and to their counsel, and there will soon be no one willing to undertake such important work. It is utterly impractical to conceive that each creditor will individually employ necessary counsel at a cost proportionately unwarranted to the amount of his claim, to guard his interests and to plan the rehabilitation of the debtor. If the effort of any party to the proceedings resulted in a preservation or conservation of assets or the enrichment of the estate out of which all the creditors will share, should one or a few pay the expense of such preservation or enrichment, or should each creditor who benefits by such result share such expense? Equity compels the answer.

We respectfully submit that in equity and justice to the appellants and particularly to the counsel for the Creditors Committee who rendered valuable services continu-

ously over a period of approximately sixteen months with resulting benefit to the estate, the order or decree of the District Court should be reversed and set aside and that an order should be made by this Honorable Court in favor of said appellants allowing said intervening petitions of the Creditors Committee and of its counsel for allowance of compensation to said counsel as an expense of administration in this estate and instructing the Receiver to pay the same out of the funds in his hands belonging to this estate.

Respectfully submitted,

SAMUEL S. GELBERG,

Attorney for Creditors Committee and Creditors Committee of Western Blind and Screen Co., Inc., a corporation, Appellants.